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In the Supreme Court of the United States

OCTOBER TERM, 1967

No. 86

UNITED STATES OF AMERICA, APPELLANT

v.

THIRD NATIONAL BANK IN NASHVILLE, NASHVILLE BANK AND TRUST COMPANY AND WILLIAM B. CAMP, COMPTROLLER OF THE CURRENCY

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF TENNESSEE

REPLY BRIEF FOR THE UNITED STATES

Appellees make three arguments that require a reply: (1) that the district court erroneously found that commercial banking was the relevant product market in which to measure the competitive effects of the merger; (2) that in determining whether the anti-competitive effects of a merger are clearly outweighed by the convenience and needs of the community, it is irrelevant that there were other methods of solving the acquired bank's problems that involved either no anticompetitive effect or a lesser one than the merger

caused;[1] and (3) that no such alternative methods of solving the problems of the Nashville Bank and Trust Company ("Nashville Bank") were in fact available, because, among other things, the Nashville Bank was below the minimum size that could attract capable management personnel.

I.

THE DISTRICT COURT CORRECTLY FOUND THAT COMMERCIAL BANKING WAS THE RELEVANT PRODUCT MARKET WITHIN WHICH TO MEASURE THE EFFECT OF THE MERGER UPON COMPETITION

On the basis of its examination of the services offered by commercial banks and by other types of financial institutions (Fdgs. 41–54, R. 116–118), the district court found that the former were sufficiently distinguishable from the latter to make commercial banking the appropriate product market in which to measure the competitive effect of the merger (R. 97–98, n. 5). In so ruling the district court followed and correctly applied *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 356–357, and *United States* v. *First National Bank & Trust Company of Lexington,* 376 U.S. 665, 667–668, where this Court, on

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[1] The Comptroller's contention (Br. 24) that the government is raising this issue for the first time in this Court is incorrect. In its trial brief in the district court (the relevant portion of which is reprinted in the Appendix), the government specifically made the point. It stated that "a bank surely should not be able to merge with a dominant and substantial competitor without a clear showing, first, that it had attempted to cure its problems without resorting to merger, and second, that it could not find a buyer with whom it did not directly compete, or one of lesser size than the contemplated buyer".

the basis of a similar analysis, had held in bank merger cases under both the Clayton and the Sherman Acts that commercial banking was the relevant product market.

The appellees challenge the district court's ruling, asserting that the fact that Section 5(b) of the Bank Merger Act of 1966, in defining the anticompetitive effects that make a bank merger *prima facie* unlawful, does not contain the phrase "in any line of commerce" which appears in Section 7 of the Clayton Act, indicates that Congress in the Bank Merger Act intended to reject commercial banking as a relevant product market and to substitute a broader market including other types of financial institutions (Comptroller's Br. 40-52; Banks' Br. 27, n. 14). The district court properly rejected the argument, pointing out that "It cannot be presumed that such an important change in established antitrust law would be made by mere omission," and that "there is really no significant legislative history to support the defendants' and intervenor's position on this point." (R. 97–98, n. 5). The relevant legislative history confirms the district court's conclusion.

On April 5, 1965 Senator Robertson introduced S. 1698 (89th Cong. 1st Sess.), which would have placed "exclusive and plenary" authority to approve bank mergers in the banking agencies,[2] which were to apply the criteria established in the Bank Merger Act of 1960. Bank mergers that the banking agencies ap-

[2] The Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Board of Governors of the Federal Reserve System.

proved would have been "relieved from the operation of the antitrust laws, including the Sherman Antitrust Act and the Clayton Act * * *." The Senate Committee on Banking and Currency rewrote the bill completely. In place of Senator Robertson's proposal to give the banking agencies exclusive authority to approve bank mergers and to confer antitrust immunity on mergers so approved, the bill that the Committee reported (drafted primarily by Senator Proxmire) merely required the banking agencies to notify the Attorney General of their approval of a bank merger, stayed the consummation of the merger for 30 days, and provided that if the Attorney General filed an "antitrust suit" during that period, the merger was to be further stayed until that suit was finally determined. If the Attorney General did not file suit within 30 days, the bill provided that "no proceeding under the antitrust laws, including the Sherman Antitrust Act * * * and the Clayton Act," could thereafter be brought against the merger.[3] The Senate on June 11, 1965, passed the bill as reported by the Committee. The Senate Bill never used the language of Section 7 of the Clayton Act, the change in which is the issue here; it referred only to "the antitrust laws" or to "the Sherman Antitrust Act and the Clayton Act."[4]

The House referred the Senate bill to its Committee on Banking and Currency which, after lengthy consid-

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[3] S. Rep. No. 299, 89th Cong., 1st Sess. 10 (1965).

[4] The text of the bill as introduced by Senator Robertson appears in Hearings on S. 1698 Before a Subcommittee of the Senate Committee on Banking and Currency, 89th Cong., 1st Sess. (1965). The bill as passed by the Senate appears at 111 Cong. Rec. 13304.

eration, reported out a very different bill which became the Bank Merger Act of 1966.[5] Under the Senate bill the banking agencies would have continued to judge bank mergers by the standards of the Bank Merger Act of 1960 and the courts to judge them by the standards of the anti-trust laws.[6] The House bill provided a single standard by which agency and court alike were to test such mergers—bank mergers "whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade," were declared to be unlawful unless their anticompetitive effects were "clearly outweighed" by the convenience and needs of the community to be served.

The first two clauses in the foregoing "effects" section are virtually identical to Section 7 of the Clayton Act, except that the latter also includes the words "in any line of commerce." The House Committee's report on the bill[7] does not refer to the absence of the words "in any line of commerce," and the debate in the House similarly is silent on that issue.[8] The members of the House apparently believed that the bill retained the existing standards under Section 1 of the Sherman Act and Section 7 of the Clayton Act for determining competitive injury.[9]

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[5] H. 12173, 89th Cong., 2d Sess. (1966).

[6] S. Rep. No. 299, 89th Cong., 1st Sess. 3 (1965).

[7] H. Rep. No. 1221, 89th Cong., 2d Sess. (1966).

[8] 112 Cong. Rec. 2440.

[9] See *e.g.*, 112 Cong. Rec. 2444 (Rep. Reuss) and 2451 (Rep. Minish).

The House passed the bill on February 8, 1966. The Senate considered and passed it the following day, without having received any report on the bill from its Committee on Banking and Currency. This was almost 8 months after the Senate had passed the earlier, and significantly different, version of the legislation.

During the extensive debate on the floor of the Senate, there was no reference to the fact that the phrase "in any line of commerce" did not appear in the bill.[10] Although Senator Robertson, in a colloquy with Senator Long of Missouri, did state that competition offered commercial banks by other financial institutions was to be considered relevant in determining whether a merger tends to lessen competition,[11] this single statement represented Senator Robertson's own views, and is not a reliable indication of the sense of the Senate. For the legislation actually enacted was written in the House, was not the subject of a report

[10] The Comptroller quotes a statement from Senator Robertson which specifically refers to the omission of the words "in any line of commerce," and indicates that such omission was intended to broaden the inquiry on anticompetitive effects to "the entire field of banking and in the broader field of financial institutions * * *" (Comptroller's Br. 48). But the statement (as well as the longer statement quoted on pages 46–48 of the brief) was not made during the debate on the floor of the Senate, but was inserted into the Congressional Record by unanimous consent—*i.e.*, it was added to the text of the actual debate when that day's Record was prepared by the printer. 112 Cong. Rec. 2653, 2655. The members of the Senate obviously were not aware of the statement when they voted on the bill that day, and it is not a relevant part of the legislative history of the Act.

[11] 112 Cong. Rec. 2664.

by Senator Robertson's Committee, and was so different from the bill he had proposed as to entitle his interpretation of the Act to little, if any, significance.

In short, there is nothing in the legislative history that provides any real support for the contention that the absence of the phrase "in any line of commerce" reflects a congressional intent to change for bank mergers the settled standard under Section 7 governing the determination of product markets. Perhaps the elimination of the words was inadvertent; or perhaps Congress concluded that in view of this Court's *Philadelphia* and *Lexington* bank cases—with which Congress was familiar [12]—it was so well settled that commercial banking is an appropriate line of commerce as to make it unnecessary to relitigate the question in future bank merger cases. Indeed, to whatever extent the legislative history sheds light upon the issue, it supports the district court's ruling. For, as noted in our main brief (pp. 21–22), the sponsors of the legislation ultimately enacted as the Bank Merger Act of 1966 stated that it embodied the settled standards of the Sherman and Clayton Acts—standards which, of course, include those used to determine the appropriate product market. Similarly this Court, in its *Houston* bank decision last term, recognized that under the 1966 Act the anticompetitive effects of a bank merger were to be "judged by the standards normally applied in antitrust actions" (*United States* v. *First City National Bank of Houston,* 386 U.S. 361, 364).

[12] See H. Rep. No. 1221, 89th Cong., 2d Sess. 4 (1966).

II.

THE ANTICOMPETITIVE EFFECTS OF A BANK MERGER ARE NOT "CLEARLY OUTWEIGHED" BY THE CONVENIENCE AND NEEDS OF THE COMMUNITY IF THE PROBLEMS OF THE ACQUIRED BANK COULD HAVE BEEN SOLVED BY SOME MEANS OTHER THAN MERGER

Appellees contend (Bank's Br. 41–47, Comptroller's Br. 34–40) that, in applying the convenience-and-needs defense of the Bank Merger Act of 1966, there is no occasion to consider whether some means other than a merger could have solved the problems of the merging bank. Although the Act does not in terms require consideration of this question, we submit that such consideration is a necessary element of the statutory directive prohibiting anticompetitive bank mergers unless their anticompetitive effects are "clearly outweighed in the public interest" by the effect of the transaction in meeting the convenience and needs of the community to be served. For although Congress was willing to permit anticompetitive mergers if "clearly outweighed" by the convenience and needs of the community, there is no indication that Congress intended to pay the unnecessarily high price that results if an anticompetitive merger is permitted when other less anticompetitive methods could equally well serve the community convenience and needs.

The principal concern of Congress in providing the convenience-and-needs defense was to permit mergers involving so-called "floundering banks," *i.e.,* those which, although not yet in failing condition, had suf-

ficiently serious problems to cause grave concern as to their future unless the deficiencies were corrected. See H. Rep. No. 1221, 89th Cong., 2d Sess. 3 (1966). Under the related failing company defense to Section 7 of the Clayton Act, a merger may be permitted on the theory that since by definition the acquired firm soon would disappear as an independent entity, its elimination does not substantially lessen competition. Even in that situation, however, it is relevant to consider whether there are alternative purchasers of the company who might continue to operate it as an independent firm (*United States* v. *Diebold, Inc.,* 369 U.S. 654, 655; *International Shoe Co.* v. *Federal Trade Commission,* 280 U.S. 291, 302). For if there are such purchasers, then the elimination of the company through merger—even though it is failing—does eliminate competition that otherwise would have continued to exist, and is illegal.

In the case of a floundering bank, the possibility of an alternative method of solving the bank's problems must also be examined, for it is a critical consideration in deciding whether the convenience and needs of the community "clearly outweigh" the merger's anticompetitive effects. Indeed, in terms of public interest the case for considering alternatives may be even stronger than in the failing company situation. For in the latter situation the existence of the alternative purchaser is significant in determining whether the merger is anticompetitive at all, and if the merger is not, there is no reason to prevent it. In the floundering bank case, however, the merger by definition is anticompetitive, since it is only then

that the defense comes into play. The question therefore is whether the anticompetitive merger should be permitted because of the community benefits it may provide by strengthening the bank and avoiding more serious future problems. If the bank's present problems can indeed be solved by some step short of eliminating it as an independent competitive entity—as we believe could have been done here (see the discussion *infra*, pp. 11–18, and in our main brief, pp. 28–32)—then resolution of these problems at an unnecessarily high cost in terms of competitive injury does not "clearly outweigh" the merger's anticompetitive effects.

The Bank Merger Act of 1966 "acknowledges that the general principle of the antitrust laws—that substantially anticompetitive mergers are prohibited—applies to banks, but permits an exception in cases where it is clearly shown that a given merger is so beneficial to the convenience and needs of the community to be served * * * that it would be in the public interest to permit it." H. Rep. No. 1221, 89th Cong., 2d Sess. 3–4 (1966); *United States* v. *First City National Bank of Houston,* 386 U.S. 361, 366. In the light of the general thrust of the Act against anticompetitive bank mergers, Congress obviously contemplated that it would be the unusual case in which community convenience and needs could validate an otherwise illegal merger. Although Congress recognized that a merger sometimes might be necessary to save a floundering bank, it certainly did not intend to sanction the elimination of competition that a merger entails if there were non-anticompetitive methods of

accomplishing the same corrective action. See 112 Cong. Rec. 2445 (Rep. Reuss).

As we now show, there is every reason to believe that Nashville Bank's problems could have been solved in due course without its elimination as an independent competitor in the already highly concentrated Davidson County banking area.

III

THE PROBLEMS OF NASHVILLE BANK COULD HAVE BEEN SOLVED BY SOME MEANS OTHER THAN THE MERGER

A. On January 13, 1964, Weaver and his associates entered into an agreeent with Hill (whose company owned the majority of the shares of Nashville Bank) and Hackworth (the president of the bank) to purchase the controlling stock interest in the bank (R. 487, 536; Fdg. 118, R. 130). The agreement followed extensive discussions between the parties during the preceding two months (R. 485, 487), in which Hill and Hackworth furnished Weaver with "fairly complete information about the Nashville Bank and Trust Company" (R. 485). The day before the agreement was signed, Weaver spent 2 to 2½ hours at the bank on Sunday afternoon and "looked over a good many operating figures * * * certain loans and so forth" and "made up [his] mind that afternoon that [he] was going forward with the purchase * * *" (R. 487).

Weaver testified that, before he decided to make the purchase, Hill and Hackworth "had discussed with me at some length the problems of Nashville Bank and Trust Company, nothing was withheld by either

one of these gentlemen" (R. 491). The sellers indicated that the "four major problems" were (1) "management," which "was without question the biggest problem"; (2) "the lack of branch banks. Mr. Hackworth and Mr. Hill advised me that it would certainly be necessary to put in a group of small branch banks to compete"; (3) "the lack of a funded pension plan and security program for the officers and the employees of the bank"; and (4) "the complete lack of automation and a computer" (R. 491). The purchase price apparently reflected these problems, for the $350 a share that Weaver and his associates paid for the stock was only 15.5 times the bank's 1963 earnings of $22.51 per share, whereas a group of Southern bank stocks referred to in an investment firm's analysis of the purchase price were selling at an average price of 18.5 times earnings (R. 501). Mr. Weaver explained that the latter stocks were not comparable, since most of the banks that were selling at a higher earnings multiple "are fully automated. They have funded pension plans. They have an adequate banking system. Their headquarters and their branches are modernized" (R. 502).

Weaver testified that although he and his associates had no intention when they made the purchase of selling the stock or merging the bank, but intended to operate it (R. 490, 512–515), when they "got into these problems in depth, we found that they were far greater than we had anticipated" (R. 515), and "that the management problem was even greater than we had thought it would be" (R. 493). It was for that reason, Weaver testified, that they "started serious discus-

sion with Mr. Fleming," the president of Third National. Weaver stated that Fleming, whom he described as "a great salesman," "sold me on the idea, and my associates, that the problems, the great problems, of this bank could best be solved through a merger with the Third National Bank; and that the best interests of the stockholders, the employees, the officers, and the Nashville community would be best served through a merger" (R. 515). Weaver acknowledged that "Fleming more than any other single person illuminated the problems of the Trust Company for [us] * * *. He certainly very forcefully brought to our attention the problems" (R. 535).

On March 11, 1964—two months after the Weaver group had entered into the purchase agreement and the very day of the closing thereunder—they agreed to merge with Third National (R. 361, 536), and the following day the boards of the two banks approved the merger (R. 361). Weaver and his associates received, in exchange for the stock they had purchased two months earlier, at approximately $350 a share, stock of Third National with a market price of between $405 and $420 a share (R. 534–536)—giving the group a total profit of between approximately $600,000 and $760,000 on its investment of $3,780,000 (R. 499).

During the 8-week interval between their purchase and sale of the stock, Weaver and his associates "talked to a great many people in the banking and financial industry about the problem of management" (R. 493) and the bank's other problems (R. 527, 537–539). They concluded that "it would be very difficult

to bring in a man to replace Mr. Hackworth," the retiring president of Nashville Bank (R. 493); that suitable locations for branch banks were difficult to secure and expensive, and that "it would be several years before we could hope to break even in a new branch bank" (R. 494); and that although Hackworth had told Weaver that in 1957 the estimated cost of funding a pension plan was $257,000, by 1964 that amount had increased to $378,000 (R. 494). The Weaver group did not seek the assistance of any management recruiting firm—because it preferred to rely upon "all of the connections that we had" (R. 531)—nor did it "speak with anybody in local business or industry exploring the possibilities of coming to work for the Trust Company" (R. 526–527). (Mr. Hackworth, who was regarded as primarily responsible for the great success the bank had had since he joined it as president in 1956, had been president of a railroad prior thereto, R. 383.)

This evidence, we submit, falls far short of establising that only a merger could have solved Nashville Bank's problems. Rather, what it shows is that the Weaver group purchased a controlling interest in the bank at a price that reflected its problems; that upon further investigation the problems turned out to be more serious, and more expensive to deal with, than the purchasers had believed, and that the purchase therefore was less attractive than it had appeared; and that they quickly liquidated their investment at a substantial profit by selling to the Third National Bank after the president of that institution had "illuminated the problems of the Trust Company for

[us]" and had "sold me on the idea, and my associates, that * * * the great problems of this bank could best be solved through a merger with the Third National Bank" (R. 515, 535).

Nashville Bank was not going downhill or on the verge of serious financial difficulties when the Weaver group purchased it. The bank's net earnings after taxes had increased between 1955 and 1963 from $99,000 to $368,000 (Fdg. 65, R. 121). During the period 1955 to 1964 it "evidenced greater rates of growth, with regard to a number of major banking functions, than any other bank in Davidson County" (Fdg. 55, R. 118), and it had a substantial increase in total assets, total deposits, demand deposits, total loans and discounts, and total current operating revenues (Fdg. 56–64, R. 118–121). Although the rate of growth slackened somewhat after 1959, this meant only that Nashville Bank was not growing as rapidly as it had; it still continued to grow in the indicia customarily used to measure a bank's economic health—with the single exception of IPC (individual, partnership and corporation) deposits, the volume of which declined somewhat between 1960 and 1964 (Pl. Ex. 1004, R. 1160).

What this record shows is a bank that admittedly had serious problems, but not so serious or incapable of another solution that the elimination of the bank as an independent competitive entity held out the only reasonable prospect for alleviating the bank's ills. The fact that the growth rate of the bank may have leveled off to the point where the bank had reached a "plateau" (Bank's Br. 9) did not require such drastic

action. Many businesses frequently have such pauses in their growth; indeed, National Bank itself apparently had a similar "plateau" between 1946 and 1956, and then moved forward with renewed vigor after Hackworth became president (R. 383–384).

The Weaver group purchased the bank as an investment with full awareness that it had substantial problems. As sophisticated business men, presumably they were aware that substantial changes would be required: new personnel would have to be found, and new capital would have to be put into the business, either by additional direct investment or through reinvesting some of the bank's substantial earnings. Instead of attempting to make such changes, however, they quickly sold out at a large profit after merely "talk[ing] to a great many people in the banking and financial industry about the problem of management" and concluding, on the basis of such discussions, that "the management problem was even greater than we had thought it would be" (R. 493; see, also, R. 527, 532, 534, 537–539).

The bank's problems stemmed from the failure of its old management to take the necessary steps to keep the bank in line with current improvements in banking practices. There is no reason to believe that infusion of new and better management and new capital by the new owners could not in time have alleviated most, if not all, of these difficulties. There is no indication that the bank was inherently unsound, that it was facing imminent or insoluble financial difficulties or dangers, or that its solvency was in any way threatened. In short, Nashville Bank

was not a "floundering bank." Even if it were, the anticompetitive effect of its elimination through merger was not "clearly outweighed in the public interest" by the fact that it solved the bank's problems. The burden of establishing the community-convenience-and-needs defense is upon the banks (*United States* v. *First City National Bank of Houston,* 386 U.S. 361, 366), and a showing that the acquired bank had made all reasonable efforts to solve its problem without resorting to a merger would go a long way in sustaining that burden. Here, however, as we have shown, the appellee banks have not made such a showing.

B. Since Nashville Bank's problems stemmed from its management, we next turn to the banks' contention (Br. 49) that Nashville Bank was "below the economic minimum size to attract capable and vigorous management personnel." The banks cite no authority for their remarkable suggestion that the twelfth largest bank in the state (out of 290, Pl. Exs. 1019, 1020, R. 1173, 1175), with total deposits of $45.5 million at the time of the merger (Fdg. 66, R. 121), was not large enough to attract competent personnel, so that a merger with a much larger bank was the only possible method of solving its management problems. The most recently published statistics of the Federal Deposit Insurance Corporation show that more than 94 percent of the nation's insured banks had total deposits of less than $50 million and more than 89 percent of such banks had total deposits of less than $25 million. Annual Report of the Federal Deposit Insurance Corporation, 1965, pp. 148–149. If the banks' assertion were sound, it would mean that the

elimination through merger of more than 90 percent of the nation's banks automatically could be justified if they had serious management problems. Congress plainly did not intend such a result in the Bank Merger Act of 1966, which was basically designed to prohibit, and not sanction, anticompetitive bank mergers.

Respectfully submitted.

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DECEMBER 1967.

APPENDIX

Excerpt From Plaintiff's Trial Brief (pp. 91–92)

Thus, before allowing a horizontal merger in cases where failure is not imminent, the agencies and courts should require banks to make good faith efforts to overcome any capital, profit, management, internal growth, or other problems. If a bank cannot improve its situation through such good faith efforts, then it should be required to seek a buyer other than a dominant bank with which it is in direct competition.[58] Only after such alternatives have been pursued to no avail should a merger that lessen competition substantially be allowed.[59]

Plaintiff contends that the "larger contours" concept written into the recent Amendment allows the proponents of an anticompetitive bank merger to justify that merger by proving that it is necessary to protect the community from the danger of an insolvent or floundering bank, but that the burden upon the defendants to establish this is an extremely heavy one. In view of the fact that Congress was primarily

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[58] Where there is more than one prospective purchaser, the comparative effect upon competition of mergers with different purchasers may be significant, and a sale to the highest bidder may violate Section 7 if a sale to a lower bidder would better fulfill Section 7 objectives. See Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics*, 74 Harv. L. Rev. 226, 346–347; Note, 68 Yale L.J. 1627, 1666–1668.

[59] Of course, if a bank is in imminent danger of failure it may be necessary to approve a merger immediately. Special provisions have been inserted in the Bank Merger Act to provide for expedited approval in such a case. See Bank Merger Act of 1966, paragraph 6.

interested in protecting competition, a bank surely should not be able to merge with a dominant and substantial competitor without a clear showing, first, that it has attempted to cure its problems without resorting to merger, and second, that it could not find a buyer with whom it did not directly compete, or one of lesser size than the contemplated buyer.